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POSTAL RATE COMMISSION
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POSTAL RATE AND FEE CHANGES, 1997

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DIRECT TESTIMONY

OF

STEVE ZWIEG

ON BEHALF OF

PARCEL SHIPPERS ASSOCIATION

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AUTOBIOGRAPHICAL INFORMATION

My name is Steve Zwieg. My address is 1655 West Rogers Drive, New Berlin, Wisconsin 53151. I am the Manager of Parcel/Direct. Parcel/Direct is a subdivision of Quad/Graphics. I have been a member of the Quad/Graphics team for sixteen (16) years. Thirteen (13) of those years were spent in the mail/distribution division of the Company. My responsibilities included operations, sales and marketing, and postal committees. From 1990 through 1996 I was the Director of Mailing Services. During that period of time Quad/Graphics built an industry leader destination entry mail program. Parcel/Direct will launch two (2) facilities in 1998, one in New Berlin, Wisconsin, and one in Martinsburg, West Virginia. My Postgraduate Studies have emphasized marketing. We are a member of the Parcel Shippers Association and I am actively involved in several working committees of the Mailers Technical Advisory Committee.

PURPOSE OF TESTIMONY

The purpose of this testimony is to demonstrate to the Commission the power of drop ship discounts such as proposed in this case to increase competition, improve efficiency and delivery times, and save money for the Postal Service and for mailers. We also hope to show the Commission that it will not work if the discounts are watered down, or if the operational rules such as minimums are dictated arbitrarily with no recognition of actual operating conditions at destination facilities.

I. DELIVERY AND SERVICE CONCERNS.

Direct marketers today are very dependent upon consistent delivery service from their parcel shipping providers. Yet, what is very much lacking is a level of parity between the competitors. Many direct marketers believe, and we agree with them, that when they shop for a consistent, reliable service they have only one option: UPS. This, of course, means that they have only one price. Certainly it should be understandable why no business wants to be held over a barrel by only one provider of an essential service. We believe that we at Parcel/Direct can provide an additional competitive option for direct marketers who are searching for an option, an opportunity that exists largely due to the DSCF discounts proposed in this proceeding.

Parcel/Direct combines the mailings of numerous customers and transports that mail to down-stream postal distribution and delivery facilities. Our company grew out of the rate incentives for destination entry that this Commission created in its recommendations in the R90-1 rate proceeding. The discounts from destination entry spawned by that decision have saved catalogers tens of millions of dollars in distribution costs, while at the same time giving Parcel/Direct the opportunity to develop a network capable of shipping fifteen million pounds of printed materials each week. Because seventy percent (70%) of this volume was transported by us to destination sectional center facilities, catalogers have experienced a higher degree of on time delivery, as well as cost savings. This is illustrated in Table 1 below. This Table shows the results of samples from our Standard A Seed Tracking Program. It rather graphically illustrates that the catalogs entered at BMC and SCF levels dramatically reduce the number of days from entry to in home delivery.

Table 1

A summary of Seed responses from July '97 through September '97 illustrates the service gains associated with entering mail at the SCF level versus BMC levels.

Quad/Graphics seed tracking program consists of 500 seeds located nation wide.

Destination entry level	Average number of days from the facility to home
BMC	7.93 days
SCF	4.67 days

Parcel/Direct's mission is to achieve these same results that were achieved for catalogs with parcel post. Through the DSCF rates Parcel/Direct will team with the Postal Service to provide a premiere residential delivery program. Parcel/Direct's docking of parcels at the SCF facility will reduce postal handling and improve the level of service to the direct mail industry. We believe that both the financial health of the Postal Service and the continued vitality of direct mail depend on the ability to achieve these results. More competition is absolutely essential in the delivery of residential parcels. DDU and SCF entry destination entry rates provide that means. Under the proposed rates in this case we estimate that 50% of the destination entry volumes will enter at the SCF. This estimate is based on actual case studies conducted for our clients. The proposed rates are what provide the economic incentive to reach this level of SCF entry. To really make it work, however, it is essential that the Commission allow the postal operations people to work with the industry to take practical advantage of the rates it will recommend.

II. THE PROPOSED RATES HOLD OUT THE PROMISE OF AFFORDABLE DELIVERY TO THE DIRECT MAIL INDUSTRY.

The success of the DBMC rate that this Commission recommended in R90-1 demonstrates that direct mailers are looking for residential delivery at a rate they can afford. Destination entry to the BMC provided the first step in that search. The core competency of the Postal Service is residential delivery. And this Commission's recommendation in R90-1 created the first opportunity for the service to aggressively employ this core competency. And the response from the industry was overwhelming. Parcel post volumes have increased sixty-five percent (65%) since the implementation of the Commission's DBMC rate recommendation. We strongly advocate the continuation of this recognition that different partners have different competencies and that a rate schedule should be designed to maximize the competencies of each of the partners in the distribution process.

Maximizing core competencies in a distribution network is neither easy nor cheap. Volume is always the decisive factor; thus, destination entry discounts must be designed to encourage those who can accumulate large masses of volume. Only in this way will the market be able to benefit from the core competencies of the industry partners. This requires a large shift in parcel volume that is directed solely to the delivery unit. Three things must happen:

1. The industry must make a substantial investment in buildings and equipment to reach the impact level necessary for SCF sortation. For example, Parcel/Direct will have to invest $45 million in 1998 in order to achieve fifty percent (50%) SCF penetration. The industry will not make investments of that size unless

there are rates recommended by this Commission that encourage mailers to make the large volume shifts to that kind of entry. Table 2 summarizes the SCF percentages that can be achieved based on volume increases. This Table shows the rapid increase in the percentage of SCF destination delivery as the volume of parcels to be shipped increases.

TABLE 2

Parcel Level	SCF%	# Parcels SCF*	# of Zips	#SCF's
50,000	6%	2,847	142	46
100,000	27%	26,943	1,226	129
200,000	51%	101,944	3,646	150

* Figures based on minimum of 30 parcels per pallet with a minimum weight of 150lbs.

We cannot emphasize too strongly how important it is that the Rate Commission not water down the discounts proposed for the different stages of drop shipping in this proceeding. If the Commission waters down the discounts it will cause more damage than good. A gradual transition with moderate discounts as a test will benefit no one. The Postal Service will not reduce its labor costs, and private distribution companies such as ours will fail to achieve the economies of scale that we must have in order to meet the downstream destinations. Unless the incentives are substantial the direct mail industry will not make the investments and take on the costs that are required to make the change. We will not see improvement in service nor will we see the affordable delivery that the industry is looking for unless this Commission creates adequate incentives. Table 3 illustrates the savings that can result with higher SCF volumes. This Table shows that a smaller minimum number of parcels per pallet and lower minimum weight produces a greater potential cost saving than do higher minimum parcels per pallet with a heavier minimum weight, because it increases the number of DSCF parcels.

TABLE 3

COMPANY	BMC (only)	BMX/SCF*		BMC/SCF**	
XYZ	$54,331.55	$51,010.10	41% SCF	$53,015.22	17% SCF
DFG	$94,580.96	$88,863.72	39% SCF	$92,422.15	17% SCF
GLT	$114,481.80	$103,666.22	38% SCF	$109,657.07	29% SCF
ABC	$279,945.32	$249,341.59	65% SCF	$264,714.35	35% SCF
TLR	$169,106.78	$125,976.14	47% SCF	$131,735.05	22% SCF

* Based on the Proposed Rates with a minimum of 30 parcels on a pallet and minimum weight of 150lbs.

** Based on the Proposed Rates with a minimum of 60 parcels on a pallet and minimum weight of 250lbs

On average these customers are savings 7% - 11% when using the BMC/SCF* service level.
These savings are reduced by 50% to 60% using the BMC/SCF** service level.

Quad/Graphics and Parcel/Direct are strong believers in the kind of public private partnership that worksharing opportunities created by this Commission in the past have offered. Quad/Graphics has spent $10 million on an Automated Storage and Retrieval System (AS/RS) to improve its ability to sort Standard A mail for entry destination SCF. Quad/Graphics wholly-owned trucking company, Duplainville Transport, has grown from a thirteen (13) unit fleet to two hundred eighty-five (285) units to support destination entry. All of this economic activity and opportunity was created when the PRC recommended the very same kind of discount levels for Standard A that the Postal Service now proposes be offered to Standard B. Because of the success of these programs, Parcel/Direct supports strongly the DSCF and DDU rate proposals in this case. Our confidence in the business direction that the Postal Service is taking parcel post has given us the confidence again to invest $45 million in plant and equipment. As with other destination entry programs, the level of service and the affordability of service provided will be greatly advanced.

This is not only good business for us but it is good business for the Postal Service. By entering forty-seven percent (47%) of its mail at DSCF rates, a mailer could reduce its costs over current rates by eight percent (8%). We illustrate this in our Table 4 with an actual example of the results that would be achieved for a customer under the Postal Service's proposal.

TABLE 4

	Service Level	
Company	**BMC (only)**	**BMC/SCF****
ABC*	$136,106.78	$125,916.14

*Customer ABC achieved an 8% saving in total cost.
ABC achieved a 47% SCF level (i.e. 47% of ABC parcels entered the postal system at the SCF level.)

** Total cost based on the Proposed Rates.

This kind of opportunity to save will ensure that current users will remain with the Postal Service. This will also give those mailers an opportunity to invest the savings back into the business which will, of course, lead to more Standard A mail and parcel shipments. And, these kinds of rates also increase competition which will lead again to an increase in residential deliveries for the Postal Service. Because the competition (UPS) continues to raise its rates for residential shipments, this creates a real opportunity through worksharing for the Postal Service to gain market share.

III. <u>VOLUME QUALIFICATIONS FOR THE DISCOUNT LEVELS</u>.

Our customers, *i.e.*, the mailers, must be able to take practical advantage of new rate categories issuing from this proceeding. The minimum volumes for destination entry rates must not be set at such a high qualification level that it is beyond the capacities of the mailers. Meeting the minimum requirements is going to require mailers to invest in sortation equipment and incur higher labor costs. Volume levels necessary to qualify should be an operational decision made jointly by mailers and postal operations people. The size and operational capabilities of a particular destination entry facility should determine the qualifying level rather than a level arbitrarily imposed by the Commission.

Parcel/Direct will focus its SCF and DDU sortation and distribution on the top four thousand (4,000) five digit zip codes. The qualification levels should be based on the operational abilities of the facilities serving those zip codes, and not on a worst-case scenario that will cover the entire national scene. Material handling equipment, dock space, transportation are all essential factors to be weighed for each destination. An example of the kind of minimum qualification that would be a disaster would be a minimum of sixty (60) parcels for a five digit pallet container. This would virtually eliminate the ability to achieve SCF rates, at least at rate levels that would meet the competition. A thirty (30) package minimum, as illustrated in Table 3, above, allows for a thirty-eight percent (38%) to sixty-five percent (65%) distribution. Whereas, a sixty (60) package minimum limits Parcel/Direct, or any other consolidator, to a seventeen 17%) to thirty-five (35%) SCF distribution.

IV. THE OPPORTUNITY FOR TRULY REMARKABLE TRANSPORTATION EFFICIENCIES

Destination SCF discounts for parcel post are an essential step in the efforts to consolidate all mail types into single shipments. As the entire direct mail industry is looking at efforts to improve delivery, nothing is more essential than efficient transportation. For example, parcel post that is combined with Standard A and periodical mail and entered at SCF destinations altogether addresses that objective. The opportunity to combine all classes of mail on the same truck will significantly reduce transportation costs and improve time of delivery. The average three stop load will become a two stop load if parcel post can be added. By reducing the number of stops the average cost for each load will be reduced by $55.00. A reduction for distance traveled accounts for another $156.00 savings. This is a combined reduction of $211.00 per load. This is illustrated in Table 5.

TABLE 5

Flat Stop Charge Scenario (Three Stops)

Load No	Stop No	Name	City	State	Weight		Stop Cost	Line Cost	Total Cost
1	1	SCF Chicago	Chicago	IL	20,000	$	55		
1	2	SCF Indianapolis	Indianapolis	IN	11,500	$	55		
1	3	SCF Louisville	Louisville	KY	11,500	$			
					43,000	$	110	$ 545.80	$655.80

Flat Stop Charge Scenario (Two Stops)

Load No	Stop No	Name	City	State	Weight		Stop Cost	Line Cost	Total Cost
1	1	SCF Chicago	Chicago	IL	27,000	$	55		
1	2	SCF Indianapolis	Indianapolis	IN	16,000	$	-		
					43,000	$	55	$ 389.47	$444.47

And, of course, there will be improvements in speed of delivery through the reduction in transit times that result from stop off delays. Products will take a more direct route to final destinations. Thus, not only will parcel shippers benefit from the proposals in this case, but so will Standard A and periodical mailers benefit as well. The increased volumes create the destination entry for all classes of mail.

V. CONCLUSION.

Parcel/Direct Quad/Graphics wants to be the leader in this industry for the destination entry worksharing program. Our business objective is to become a partner with the Postal Service so that together we can improve their bottom line and the bottom line of every direct mailer. We have no doubts that, if the Commission will provide the leadership necessary to create these worksharing opportunities, the Postal Service can have significant growth and become a major competitive factor. We are so confident of that we are spending $45 million on our first two facilities in New Berlin, Wisconsin and Martinsburg, West Virginia. The New Berlin facility will be a 360,000 square foot distribution facility with the ability to sort 200,000 packages per day. The West Virginia facility will be a 400,000 square foot distribution facility with the ability also to sort 200,000 packages per day. Whether these operations are successful depends completely upon what the PRC recommends in this proceeding. We cannot justify this investment if the Commission waters down the proposed SCF rates; and the qualification levels must be decided at an operational level based on the ability of the facilities that are affected, and not imposed in the absence of marketplace realities by the Commission, or by Postal Service Headquarters for that matter.

CERTIFICATE OF SERVICE

I hereby certify that I have this date served the foregoing upon all participants of record in this proceeding in accordance with Section 12 of the Rules of Practice.

Timothy J. May

Dated: December 29, 1997